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SUBJECT: TRADE MINISTRY CONSIDERING MARKET-ORIENTED APPROACH WITH PDS IMPLICATIONS

¶1. (SBU) Summary and Comment: Two reform proposals originating from within the Iraqi Ministry of Trade (MoT) would liberalize state control over food production and processing. The first deals with Iraq's corrupt and inefficient food rationing program, the Public Distribution System (PDS). The proposal would privatize flour milling and could positively impact \$700 million in existing U.S. wheat sales. The second is a possible sharing of MoT grain handling facilities for private imports of animal feeds and other commodities. It is too early to gauge the GOI's commitment to implementing either proposal, but that these steps are being considered at all is encouraging. End Summary and Comment.

Wheat Flour & Rice Reforms

¶2. (SBU) High-level officials at the Ministry of Trade (MoT) and its purchasing arm, the Iraqi Grain Board (IGB), are discussing significant changes to the Public Distribution System (PDS). These changes, if instituted, could be positive steps toward market orientation. Under discussion is a plan that would reduce the PDS allotment of wheat flour and rice given to each Iraqi. This component of consumer demand would, in the future, be met by the private sector. We are seeking copies of both plans from the MoT contact who briefed us on the details of the plans.

¶3. (SBU) Virtually all Iraqi private sector flour mills are under exclusive contract with the MoT to mill flour for the PDS. Most mills are outdated and operate at only 25-50% of their rated capacity. Under this plan, flour mills could choose to be released from PDS milling contracts thereby becoming genuinely private sector entities or renegotiate/bid competitively for new PDS contracts. The plan as envisioned would act as a catalyst to allow the re-emergence of a private sector milling industry.

¶4. (SBU) The MoT is exploring similar options for the other major PDS commodities including rice, sugar, and vegetable oil, as first steps toward possible disengagement from supplying state-rationed food to Iraqis. This type of reform could also provide a boost to retail food shops that currently compete against free food commodities distributed through PDS agents throughout the country. Private Use of MoT Grain Handling Facilities

¶5. (SBU) MoT has also indicated that they will consider facilitating the import and distribution of feed grain commodities (corn, sorghum, soybeans, and protein meals) to the private sector through the use of their existing infrastructure. Most feed is currently imported by truck from Syria or Turkey whereas transportation by ocean-going vessels would be much more efficient if the private sector had access to port facilities in Umm Qasr. The initiative is significant because the lack of availability and high price of animal feed continues to hinder Iraq's agricultural economy and results in reduced agricultural employment and higher meat and poultry prices. Significant demand exists for imported corn, soybeans, and other feed components. However, the Ministry of Agriculture maintains a thicket of procedural import barriers and seasonal import bans that make Iraqi feed prices the region's highest. We do not believe that the Ministry of Agriculture is aware of the MoT plans yet.

¶6. (SBU) Comment: The wheat plan would significantly reduce the "crowding out" effect of the PDS, and could re-establish a private milling sector, while concurrently reducing one of the main avenues for corruption in the PDS structure. If handled correctly, it could reduce corruption in the PDS structure. If handled correctly, it could also greatly improve the range and quality of flour available to the Iraqi baking industry. Newly privatized domestic millers could recapture the market niche now filled by state-supported imports of flour from Turkey. We estimate that one-third of the PDS flour is now illicitly resold into the private market. The plan would reduce this "leakage," eliminating a huge and expensive inefficiency inherent in the current PDS design. Regarding the use of MoT handling facilities for private feed imports, Iraq's livestock sector would reap huge benefits from bulk feed grain imports, through much lower feed cost. Increasing the feed supply has been an ongoing objective for a range of U.S. policy and development initiatives. This may create an opportunity for USDA-sponsored initiatives in the areas of private/public sector procurement strategies and milling science. End Comment.